SUPREME COURT OF THE UNITED STATES.

OCTOBER TERM, 1914.

No. 99.

GLOBE BANK AND TRUST COMPANY OF PADUCAH, KENTUCKY, APPELLANT,

vs.

ARTHUR Y. MARTIN, TRUSTEE IN BANKRUPTCY OF THOMAS JEREMIAH ATKINS, APPELLEE.

No. 100.

FIRST NATIONAL BANK OF PADUCAH, KENTUCKY, APPELLANT,

vs.

ARTHUR Y. MARTIN, TRUSTEE IN BANKRUPTCY OF THOMAS JEREMIAH ATKINS, APPELLEE.

No. 101.

OLD STATE NATIONAL BANK OF EVANSVILLE, INDIANA, APPELLANT,

vs.

ARTHUR Y. MARTIN, TRUSTEE IN BANKRUPTCY OF THOMAS JEREMIAH ATKINS, APPELLEE.

BRIEF FOR APPELLEE IN EACH OF THE FOREGOING CAUSES.

ARGUMENT.

Without appearing to be arguing elementary propositions of law, but in reply to the brief of counsel for appellant, we take up and wish to discuss the nature of the asserted liens

upon the property of the bankrupt in the action of the State Court under the Kentucky Statutes, and their relation to the provisions of the Bankruptcy Act.

Section 70*a* is as follows:

> "The trustee of the estate of a bankrupt, upon his appointment and qualification, and his successors, if he shall have one or more, upon his or their appointment and qualification shall in turn be vested by operation of law with the title of the bankrupt, as of the date he was adjudged a bankrupt, except in so far as it is to property which is exempt, to all—(4) property transferred by him in fraud of his creditors; (5) property which prior to the filing of the petition he could by any means have transferred or which might have been levied upon and sold under judicial process against him."

Section 70*e* of the Bankruptcy Act is as follows:

> "The trustee may avoid any transfer by the bankrupt of his property which any creditor of such bankrupt might have avoided, and may recover the property so transferred, or its value, from the person to whom it was transferred, unless he was a *bona fide* holder for value prior to the date of the adjudication. Such property may be recovered or its value collected from whoever may have received it, except a *bona fide* holder for value. For the purpose of such recovery any court of bankruptcy as hereinbefore defined, and any State Court which would have had jurisdiction if bankruptcy had not intervened, shall have concurrent jurisdiction."

The section and its subsection absolutely fixed that title which Congress intended should be vested in the trustee in bankruptcy upon the adjudication and their language is very plain and explicit. In the case at bar we presume it will be conceded that the bankrupt, Atkins, transferred the property involved in the proceeding in the State courts, in actual or constructive fraud of his then existing creditors; if otherwise then his creditors would have had no cause of action.

Section 70*e* explicitly provides that the trustee may avoid *any transfer* by the bankrupt which any creditor might have avoided and it provides the forum in which such action may be brought. In the case at bar the forum having been chosen by the antecedent creditors of the bankrupt, prior to the adjudication, the trustee then availed himself of an independent action brought for the same uses and purposes and which action was thereafter consolidated with the then existing actions of the various banks.

The litigation in the State Court and the effect of the opinion of the Court of Appeals of Kentucky, has been ably argued in the brief of counsel for appellee.

If the title to the property conveyed in fraud of any creditor vested in the trustee, or if the right to proceed vested in any creditor, then the provisions of section 67*f* apply, and all of the steps required under that section for the purpose of obtaining the benefits of the legal proceedings for the subjection of the property of the bankrupt were preserved to the trustee.

Section 67*c*, Bankruptcy Act, is as follows:

> "A lien created by or obtained in or pursuant to any suit or proceeding at law or in equity, including an attachment, upon mesne process or a judgment by profession, which was begun against a person within four months before the filing of a petition in bankruptcy by or against such person shall be dissolved by the adjudication of such person to be a bankrupt if (1) it appears that said lien was obtained and permitted while the defendant was insolvent and that its existence and enforcement will work a preference, or (2) the party or parties to be benefited thereby had reasonable cause to believe the defendant was insolvent and in contemplation of bankruptcy, or (3) that such lien was sought and permitted in fraud of the provisions of this act; or if the dissolution of such lien would militate against the best interests of the estate of such person the same shall not be dissolved, but the trustee of the estate of such person, for the benefit of the estate, shall be subrogated to

the rights of the holder of such lien and empowered to perfect and enforce the same in his name as trustee with like force and effect as such holder might have done had not bankruptcy proceedings intervened."

Section 67*e*, Bankruptcy Act, is as follows:

"That all conveyances, transfers, assignments, or incumbrances of his property, or any part thereof, made or given by a person adjudged a bankrupt under the provisions of this act subsequent to the passage of this act and within four months prior to the filing of the petition, with the intent and purpose on his part to hinder, delay, or defraud his creditors, or any of them, shall be null and void as against the creditors of such debtor, except as to purchases in good faith and for a present fair consideration, and all property of the debtor conveyed, transferred, assigned, or encumbered as aforesaid shall, if he be adjudged a bankrupt, and the same is not exempt from execution and liability for debts by the law of his domicile, be and remain a part of the assets and estate of the bankrupt and shall pass to his said trustee, whose duty it shall be to recover and reclaim the same by legal proceedings or otherwise for the benefit of the creditors. And all conveyances, transfers, or encumbrances of his property made by a debtor at any time within four months prior to the filing of the petition against him, and while insolvent, which are held null and void as against the creditors of such debtor by the laws of the State, Territory, or District in which such property is situate, shall be deemed null and void under this act against the creditors of such debtor if he be adjudged a bankrupt, and such property shall pass to the assignee and be by him reclaimed and recovered for the benefit of the creditors of the bankrupt. For the purpose of such recovery any court of bankruptcy as hereinbefore defined, and any State Court which would have had jurisdiction if bankruptcy had not intervened, shall have concurrent jurisdiction."

Counsel for appellant rely upon the opinion of the Circuit Court of Appeals for the Sixth Circuit in the case of *In re*

Bennett as conclusive of the issues of the case at bar. There is a vast distinction between the liens accorded under section 2487 *et seq.*, Kentucky Statutes, and the liens acquired by the antecedent creditors of the bankrupt in this case.

Liens accorded under section 2487 *et seq.* are statutory liens given to mechanics and materialmen and arise by operation of law upon the happening of the contingencies mentioned in the statute. If the creditor presents his claim and claims this lien, as was said in *In re* Bennett, the lien may not be defeated by alienation act of the bankrupt or even death itself, but attaches to the *res* and the court administering the estate upon which the lien exists will respect and enforce it. It is essentially a lien accorded by statute and is differentiated from the lien acquired by legal proceedings, such as we have in this case.

The lien of the antecedent creditors in this case was created by, and obtained in a suit or proceeding in equity, begun against the bankrupt within four months before the filing of the petition in bankruptcy. It was an attachment upon mesne process, and if it be argued that the attachment was unnecessary, under section 1907*a* Kentucky Statutes, yet it was a lien upon mesne process, and, *ipso facto,* by adjudication of the bankrupt dissolved.

Cyc., volume 25-662, recognizes three classes of liens, the latter two of which it defines as equitable liens and statutory liens.

Section C:

> "An equitable lien is one which a court of equity recognizes as distinct from strictly legal rights, and is always ready to enforce regardless of what rights the applicant may have in a court of law. The term 'equitable lien' merely denotes a charge or encumbrance of one person upon the property of another. It is not a right of property in the subject-matter of the lien nor a right of action therefor, nor does it depend upon possession; but is merely a right to have the property subjected to the payment of a debt or claim, and it applies as well to charges arising by

express engagement of the owner of property as to a duty or intention implied on his part to make the property answerable for a specific debt or engagement."

Hines *vs.* Duncan, 58 American Rep., 580.
Peck *vs.* Jenness, 7 Howard, 612.
Shakers' Society *vs.* Watson, 15 C. C. A., 632.

The lien acquired by the antecedent creditors in this action falls under the head of equitable liens, as defined above. Provisions of the Kentucky Statutes merely declare the law, and Sec. 1907*a* merely provides for an adequate remedy.

Statutory liens are defined in the authority above quoted as follows:

Section D:

"Liens are also frequently defined or provided for by statute. Such statutes embrace in a modified form the common-law liens, and also frequently provide for liens in cases to which the common-law lien does not apply. Statutory liens, however, have been looked upon with jealousy, and generally will only be extended to cases expressly provided for by the statute, and then only where there has been a strict compliance with all the statutory requisites essential to their creation and existence. A statutory lien is provided for not only where the statute expressly declares that under certain circumstances a person shall have a lien upon a certain class of property for a debt or charge due, but also where it declares that a person shall have the right under given circumstances to hold certain property for or subject to the payment of a certain claim or charge, even though the word 'lien' is not used in the statute."

The liens enforced in the case of *In re* Bennett were statutory liens accorded various creditors who were mechanics and materialmen and who claimed under the provisions of section 2487 *et seq.*

In the happening of the contingencies provided for in section 2487 *et seq.* if the creditor was within the provisions

of those sections, then the lien attached to the *res* as a matter of right; if the judgment is rendered, or if the claim was sustained, then the lien was an incident to the debt.

The equitable liens acquired by the proceedings begun by the antecedent creditors in this matter were liens which the McCracken Circuit Court, as a court of equity, recognized and established as distinct from the legal rights of the plaintiffs.

In an action under section 1907 plaintiff, to secure the lien upon the property voluntarily conveyed, was required to prove that his debt was antecedent to the conveyance and that the conveyance without consideration thereby militated against his rights. In the case of Enders *vs.* Williams, 1 Metcalf, 346, it is said:

> "A distinction, however, has been made, so far as creditors are concerned, between a voluntary conveyance to the grantor's children and to strangers. In the former case, where there is no actual fraudulent intent, and the gift is a reasonable advancement to the child, considering the donor's condition in life, and there is ample estate left unincumbered for the payment of his debts, then such conveyance will be valid, even against antecedent creditors."

To the same effect is the case of Trimble *vs.* Ratcliffe, 9 B. Monroe, 514.

Liens acquired by the appellants in this matter were acquired by operation of law, and not by a right accorded under the statute, and are within the four months' provision.

The statutory lien, when it once attaches to the *res,* may not be defeated by any act of the parties, but the very language of section 1907 shows that the lien of this character may be defeated by act of the fraudulent vendee. The very institution of the equitable proceeding creates the *lis pendens* lien, and no lien attaches to any property so fraudulently conveyed, unless and until the creditor takes action.

In the case of Lyne, &c., *vs.* Bank of Kentucky, 5 J. J.

Marshall, 553, a case decided in 1831, the statute then being almost similar to section 1907, it is said:

> "It may safely be laid down as a correct rule at common law, as well as under the statutes of 13th and 27th Elizabeth, and our statute of frauds, that all voluntary conveyances made by grantors at a time they were oppressed by debts are ineffectual to vest property in the grantee so as to prevent antecedent creditors from subjecting it to the payment of their debts; provided, the property conveyed or transferred was of that description and character which the law made liable to the payment of the debts, had the conveyance never been made."

If this lien then only attached to the property fraudulently conveyed upon the institution of the action, it arose by operation of law, and not by statute, and comes within the provisions of section 67*c*, and was dissolved by the bankruptcy.

Again, section 1907 declares and amplifies a right of action, in which, prior to the Act of 1893 (section 1907*a*), it was necessary for the plaintiff to either procure a return of a *nulla bona*, or take an attachment against the property involved. This Act of 1896 allowed the *lis pendens* lien upon the filing of the petition with the necessary averments, but there is a further statute of the State of Kentucky, section 2358, which is as follows:

> "That no action, cross-action, counter-claim, or other proceeding whatever (save actions for forcible detainer or forcible entry or detainer) hereafter commenced or filed in which the title to, or the possession or use of, or any lien, tax, assessment, or charge on real estate, or any interest therein, is in any manner affected or involved, nor any judgment or order therein, nor any sale or other proceeding thereunder, shall in any manner affect the right, title or interest of any subsequent purchaser, lessee or incumbrancer of such real estate or interest for value and without notice thereof, except from the time when there shall be filed in the office of the clerk of the county in which such real estate, or a

greater part thereof lies, a memorandum stating (one) the number of said action where the action is numbered, and style of such action or proceeding and the court in which it is commenced, or is pending; (two) the name of the person whose right, title, interest in, or claim to, real estate is involved or affected; (three) a description of the real estate in said county thereby affected.

"The requirements of the section were complied with by appellant in case No. 430 (Transcript of Record, p. 62).

From the foregoing we confidently contend that the lien acquired by the appellants in this matter was one acquired by operation of law, obtained in or pursuant to a suit or proceeding in equity and being within the four months before the adjudication of bankruptcy of T. J. Atkins, it was, as to his trustee in bankruptcy, dissolved, except in so far as it was presented to the trustee for the benefit of the bankrupt estate, and all of the creditors of the bankrupt.

Respectfully submitted,

J. W. MOCQUOT,
Attorney for Trustee.

W. F. BRADSHAW,
Of Counsel.

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No. 292.

ARTHUR Y. MARTIN, TRUSTEE IN BANKRUPTCY OF THOMAS JEREMIAH ATKINS, ET AL., PETITIONERS,

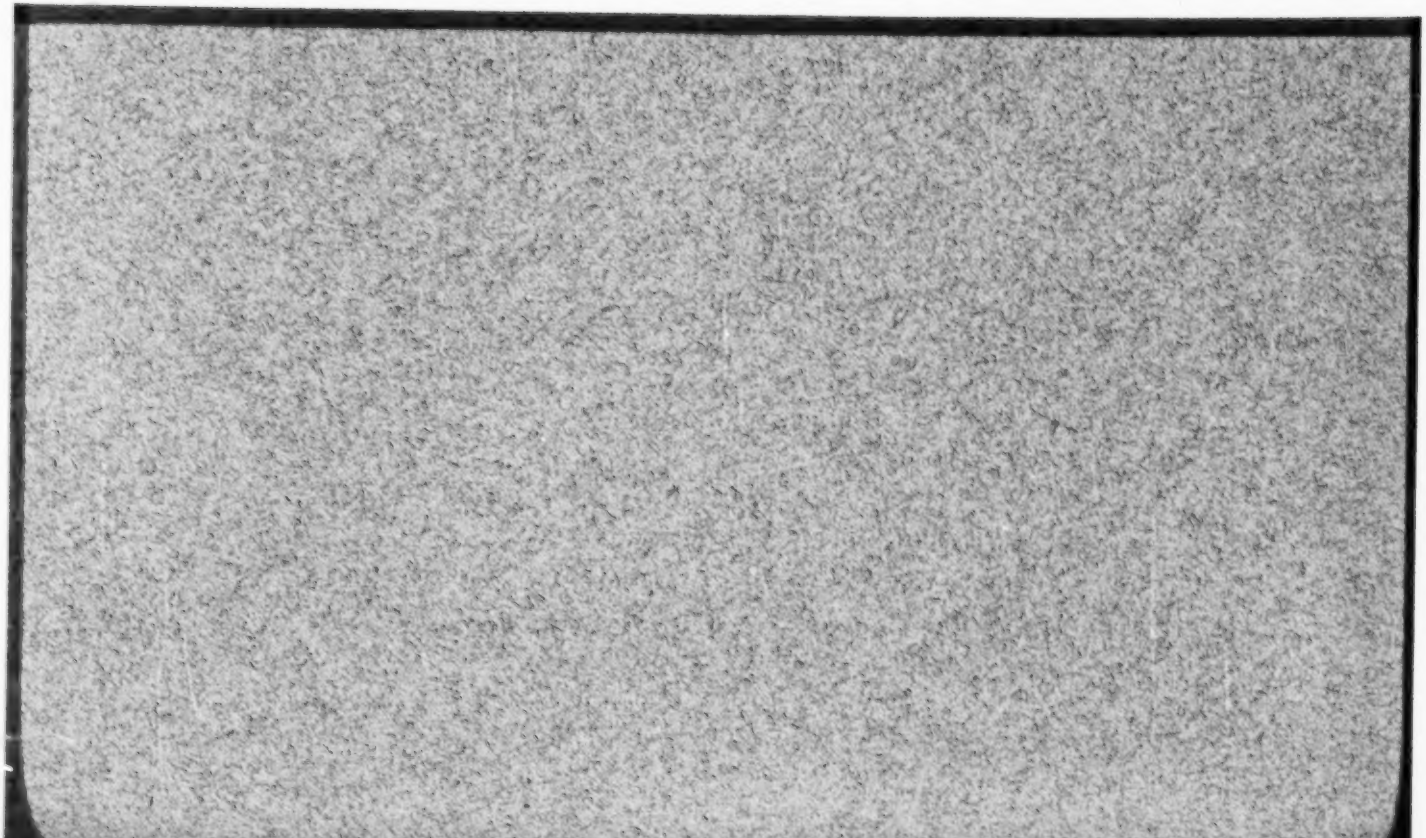
vs.

GLOBE BANK & TRUST COMPANY OF PADUCAH, KENTUCKY, ET AL., RESPONDENTS.

BRIEF FOR APPELLEE IN Nos. 99, 100, 101, AND PETITIONERS IN No. 292.

W. F. BRADSHAW, JR.,
BRADSHAW & BRADSHAW,
Attorneys for the Appellee and Petitioners for Writ of Certiorari.

J. D. MOCQUOT,
Of Counsel.



SUBJECT INDEX.

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Statement.

The statement of facts contained in the appellants' brief is incomplete and to some extent erroneous, and for that reason the following statement is submitted as embodying a more complete presentation of the facts of the record:

On December 4, 1906, Thomas Jeremiah Atkins conveyed various parcels of real estate situated in McCracken County, Kentucky, to his son, Ed. L. Atkins, and to his son's children. At the time the conveyance was made Atkins was indebted to the appellants, Globe Bank & Trust Company, First National Bank, and Old State National Bank, in sums aggregating over twenty thousand dollars ($20,000). After the execution and delivery of the deed the bankrupt incurred other indebtedness. The indebtedness to the three appellant banks will be referred to hereinafter as the antecedent indebtedness and the appellants as the antecedent creditors. The indebtedness created after the execution and delivery of the deed will be referred to hereinafter as the subsequent indebtedness and those creditors as the subsequent creditors.

During the months of August and September, 1908, the appellants instituted actions in the McCracken Circuit Court, a State court of Kentucky, seeking to set aside the deed of conveyance as fraudulent and to subject to the satisfaction of their debts the property conveyed, and at the time of the institution of the three separate actions each of the appellants had attachments issued and levied upon the property sought to be recovered.

On December 28, 1908, Atkins was adjudicated an involuntary bankrupt under proceedings in bankruptcy in-

stituted by creditors within four months of the commencement of the proceedings in the State court. Two sections of the Statutes of Kentucky were relied upon by the appellants in their actions in the State court, *i. e.*, section 1906, Carroll's Kentucky Statutes, edition 1903:

> "Every gift, conveyance, assignment or transfer of, or charge upon any estate, real or personal, or right or thing in action, or any rent or profit thereof, made with the intent to delay hinder or defraud creditors, purchasers or other persons, and every bond, or other evidence of debt given, action commenced, or judgment suffered, with like intent, shall be void, as against such creditors, purchasers and other persons. This section shall not affect the title of a purchaser for valuable consideration, unless it appear that he had notice of the fraudulent intent of his immediate grantor or of the fraud rendering void the title of such grantor."

And section 1907, Carroll's Kentucky Statutes, edition 1903:

> "Every gift, conveyance, assignment, transfer or charge made by a debtor, of or upon any of his estate, without valuable consideration therefor, shall be void as to all his then existing liabilities, but shall not, on that account alone, be void as to creditors whose debts or demands are thereafter contracted, nor as to purchasers with notice of the voluntary alienation or charge; and though it be adjudged to be void as to a prior creditor, it shall not therefore be deemed to be void as to such subsequent creditors or purchasers."

On January 9, 1909, the Globe Bank & Trust Company filed a petition before the United States District Court for the Western District of Kentucky, wherein the bankruptcy proceeding was pending, setting up the proceedings instituted by it in the State court, including an allegation specifically alleging a lien by reason of its attachment, and challenging the jurisdiction of the district court to hear or

determine any question affecting the rights of the Globe Bank & Trust Company to the property or the proceeds arising therefrom which it was seeking to recover in the State court, but in the petition prayed that the court direct the trustee in bankruptcy to join with the petitioner in the effort to recover the property for the benefit of the attaching creditors (Record, pp. 33-36).

On January 20, 1909, before action was taken by the district court on this petition, the Globe Bank & Trust Company filed another petition in the district court setting forth certain other proceedings in respect of the State court suit, reaffirming its lien by reason of the attachment and pleading, also that in order to secure the priority of its *lis pendens* lien it had notice of such lien recorded in the office of the clerk of the McCracken County Court, the register of deeds, thereby under the Kentucky law establishing such lien by a recorded notice. In this petition the appellants prayed, "that its rights and equities acquired in such action be thus fully preserved and protected in full force and effect as against T. J. Atkins and all parties claiming under or through him by this court until such action is so prosecuted to final judgment, and until the proceeds so recovered for the benefit of this petitioner and for the bankrupt's estate and the other creditors, if any, who may be entitled to share with it in such proceeds shall have finally determined a distribution of the assets of the bankrupt by this court" (Record, pp. 61-67).

Thereafter on February 18, 1909, the district court entered an order directing "that any right or lien acquired by attachment, *lis pendens* or otherwise upon any property or interest of the bankrupt be preserved for the benefit of the bankrupt's estate as provided in section 67*f* of the bankruptcy act," and also in said order directed the trustee to institute an action for the recovery of said property or to implead in the actions then pending in the McCracken Circuit Court. Shortly after the entry of the order the trustee, obedient to the order of the district court, instituted an

action in the McCracken Circuit Court for the recovery of the property, and his action was, on motion of the appellants, consolidated with their three actions (Record, pp. 36-37).

Meanwhile, before the institution of the action by the trustee the appellants had filed their proofs of claim before the referee for the same debts upon which their suits were pending in the McCracken Circuit Court. The Old State National Bank in its proof of claim stated that it did not have nor had received any manner of security for said debt whatever (Record, pp. 28-29).

The First National Bank in its proof made the same statement (Record, p. 30).

The Globe Bank & Trust Company stated that it did not have nor had received any manner of security for its debt whatever except three collateral notes described in the proof and which are not involved herein, and further stated that, "an action is pending in the McCracken Circuit Court on such notes filed August 25, 1908, under which a lien is acquired and held on the real estate therein described attacking a deed as fraudulent" (Record, p. 27).

No order was ever made by the referee either allowing or disallowing any of the claims of appellants either in respect of their original proofs of claims or any amended proofs except the final order of the referee holding that the fund in contest belonged to the appellant banks by virtue of their rights existing under any liens acquired by their acts under the laws of Kentucky (Record, pp. 91-92).

No further steps were taken in the bankruptcy proceeding affecting the question here involved pending the outcome of the litigation in the State court. The McCracken Circuit Court adjudged the conveyance was fraudulent and voidable as to antecedent creditors and entered a judgment charging the property in the hands of the vendees with a sum equal to the antecedent indebtedness, but held the conveyance good as to subsequent creditors. In the judgment the court appointed the trustee in bankruptcy as

special commissioner of the McCracken Circuit Court, with authority to sell the property, or so much thereof as might be necessary, in order to realize the sum adjudged against it, and (Record, p. 16),

> "to collect the proceeds of sale so soon as the bonds are due and hold all of the proceeds subject to the final orders of this court in the further and final disposition of such proceeds, or subject to the District Court of the United States for the Western District of Kentucky in the matter of T. J. Atkins, bankrupt, now pending in such court under its final distribution of the entire assets of the estate of such bankrupt in the final adjustment and settlement of all its affairs before such court in such proceedings now pending therein in bankruptcy, and the rights of all creditors in such bankrupt proceedings in the distribution or disposition of such proceeds by the bankrupt estate are hereby reserved and not determined, but left open for final adjudication among them in such proceeding in bankruptcy."

Both the trustee and the vendees, defendants in the State court action, appealed to the Kentucky Court of Appeals. The trustee appealed because the order of the McCracken Circuit Court directed the proceeds of the sale to be held,

> "subject to the final orders of this court in the further and final disposition of such proceedings or subject to the District Court of the United States for the Western District of Kentucky in the matter of T. J. Atkins, bankrupt."

The trustee's objection being to the alternative direction contained in the judgment, and in his appeal he sought to have the fund paid over to him as trustee in bankruptcy to be distributed by the bankrupt court alone.

The vendees, defendants in the action in the State court, appealed on the whole case; that is, on the findings of the court that the deed was in any respect fraudulent or voidable.

The Court of Appeals affirmed the judgment of the circuit court and construed the judgment, as contended by the trustee, to mean that the fund should be paid over to the trustee in bankruptcy to be administered as a part of the bankrupt estate. In passing upon the appeal of the trustee the court said (Record, p. 23):

> "The judgment does not undertake to dispose of the proceeds that may be realized from the sale of the property, but leaves this question open for future determination and we do not doubt that when the court comes to make an order concerning the disposition of the proceeds in the hands of the trustee as special commissioner, it will direct that the proceeds be paid over to the trustee in bankruptcy to be administered as a part of the estate of the bankrupt in the bankruptcy court. In anticipation of what we assume the court will do, we may, with propriety in this opinion, direct that it make such orders. If the court in the judgment had undertaken to divest the trustee of the control of this fund, we would upon this point reverse the judgment, with directions to proceed as indicated, but as the court did not make such an order we are of the opinion that on the appeal of the trustee the judgment of the lower court should be affirmed."

On the appeal of the vendees the judgment was reversed because of an error in fixing the date of the delivery of the deed. The court held, in fact, that the deed was delivered at a date subsequent to December 4, 1906, and that one of the debts sued on by the Globe Bank & Trust Company was created subsequent to December 4, 1906, and the judgment was reduced $1,285, the amount of such subsequently created debt; in other respects the judgment of the lower court was affirmed, leaving the property charged with about $20,000 of antecedent indebtedness. In passing upon the appeal of the vendees the court said (Record, p. 24):

> "To what extent this will affect the judgment creditors, we are not advised; but only those credit-

> ors whose debts were created previous to December 4, 1905, are entitled to participate in the proceeds realized from the sale of the property. If the proceeds amount to more than sufficient to pay such debts, the surplus should be paid to the grantees in the deed."

Under the mandates of the Court of Appeals the circuit court entered judgment in favor of the banks in the same sums as were entered in its former judgment in June, 1909, less $1,285 from the judgment of the Globe Bank & Trust Company, and as to the other debts sued on it was adjudged that:

> "The deed is not fraudulent but is valid as provided and adjudged in the former judgment rendered in these consolidated cases on June 19, 1909, as aforesaid, and that no trust for the payment of any of such debts so created subsequent to the deed is herein declared or adjudged.
>
> "It is now further adjudged that the proceeds arising from the sale of the property described in the former judgment rendered June 19th, 1909, aforesaid shall be held by Arthur Y. Martin, trustee, and as special commissioner of this court under the terms and conditions of such former judgment until disposed of and distributed as is directed in such judgment" (Record, p. 26).

The property having been sold by the trustee as special commissioner realized a sum less than the antecedent indebtedness with which it was charged. After the sale of the property a report to the referee was made by the trustee of the fund in his hands; each of the appellants filed supplemental and amended proofs of claim setting up the various proceedings had in the State court above enumerated and claiming that by reason of such proceedings they had a prior and superior claim upon the fund and were entitled to the full amount thereof to the exclusion of other creditors of the estate of Atkins (Record, pp. 38-46).

The trustee traversed these various petitions and amendments, claiming the fund for the benefit of the estate generally (Record, pp. 46-49).

The referee on May 23, 1910, entered an order finding that the appellant banks were the only creditors of the bankrupt whose debts existed at the date of the delivery of the deed; that the proceeds derived from the sale of the property were insufficient to pay their debts; and that they were entitled to the entire fund and directed the trustee to pay the same to them pro rata upon their respective debts. Upon petition of the trustee for review this order was affirmed by the district court; the district court holding that the voluntary conveyance though voidable as to the then existing creditors of the bankrupt was not so as to the creditors whose debts were created after the deed was delivered; also,

> "That the *lis pendens* liens and the attachments in the suits in the State court were under order of this court entered herein on February 18, 1909, preserved for the benefit of the estate."

and, further,

> "That the construction of the Kentucky Statutes by the Court of Appeals in the cases referred to is binding upon this court, even if it did not (as it does) agree with the decision" (Record, pp. 51-52).

From the judgment of the district court the trustee and certain subsequent creditors sought a review by a proceeding for a superintendence and revision in matter of law under section 24*b* of the bankruptcy act. Following this, and within six months from the date of the entering of the order of the district court, the trustee appealed from the judgment to the Circuit Court of Appeals under section 24*a* of the bankruptcy act. The appeal and the revisory proceeding were considered together by the Circuit Court of Appeals, no issue having been raised by the appellant banks to either of the methods of review sought by the trustee and creditors.

The opinion of the Circuit Court of Appeals appears at pages 73-72 of the record, in which the action of the district court was reversed and the fund directed to be taken by the trustee for distribution generally among the creditors of the bankrupt estate. Following the entry of the decree of the Circuit Court of Appeals, the appellants made various motions looking to a modification of the decree and preparation of the record for appeal to this court (Record, pp. 88-93). Upon further hearing of the cases the Circuit Court of Appeals rendered a second judgment (Record, pp. 94-100) sustaining its jurisdiction on the appeal and affirming its judgment theretofore rendered and dismissing the petition, but in so doing the court stated (Record, p. 99):

> "It cannot escape observation that grave doubts arise in the practice, as also in the courts, as to what one of the appellate remedies should be adopted for reaching courts of appeals; and although counsel for the trustee ask the court to retain the petition to revise until the Supreme Court can pass upon the other questions of remedy we think we are bound to grant the motion to dismiss that petition; but we do so with the consciousness that any error committed in this respect can be rectified through writ of certiorari."

From the judgment of the Circuit Court of Appeals the appellants have taken this appeal to this court. As a precautionary measure in order to save the rights of the trustee in the event of error on the part of the Circuit Court of Appeals in sustaining its jurisdiction on the appeal and dismissing the petition for review, the trustee and the creditors who sought review in the Circuit Court of Appeals have filed a petition for a writ of certiorari in this court.

The appeal in this court and the certiorari involve the same facts and the same case. The question of remedy will be discussed in this brief, as counsel assume that the two proceedings will be heard together.

ARGUMENTS.

The appellants raise the question of jurisdiction of this court on both the appeal and the writ of certiorari. The same question was raised at the final hearing before the Circuit Court of Appeals; that is, that the trustee should have appealed to the Circuit Court of Appeals within ten days under section 25*a* of the bankruptcy act upon the theory that the order of the district court was one rejecting a claim of $500.00 or over. At the time of the argument before the Circuit Court of Appeals the record contained no order showing an allowance or disallowance of any of the claims filed by the appellants. Appellants contended that such an order existed, but had been omitted from the record. In fact, no such order was ever made, and before entry of the final decree of the Circuit Court of Appeals a stipulation was entered into between all the parties to this appeal, and which appears at page 92 of the record in part as follows:

> "That no order was made or appears in this bankruptcy proceeding in the original record in the office of the referee or of the district court, where the proceedings in bankruptcy were instituted, allowing or disallowing any of the claims filed by the respondents and appellees, either in respect of their original proofs of claim, or of the amended proofs or petitions of said banks, except the order of the referee of date May 23, 1910, which appears at pages 56, 57, and 58 of the record.
>
> "And it is further agreed by the parties hereto that this stipulation shall be considered as a part of the record in the two above-entitled cases."

In commenting upon this contention the Circuit Court of Appeals said:

> "It is enough to say now that neither the order of the referee nor the final decree of the court below pur-

ported to be an allowance of the debt or claim, as such, of any of these three banks. Indeed the debts as originally proved do not appear to have been questioned; that the sums so ordered to be paid on such claims were each materially less than the respective debts proved. The true analysis of the order is that it was an order of distribution. It was an order to distribute a fund derived from the recovery and sale of real estate, the conveyance of which has been made by the bankrupt in fraud of the rights of certain of his creditors as pointed out in our original decision. This fund was so acquired in pursuance of an order of the bankruptcy court; and the validity of the order distributing the fund cannot, we think, be rightly tested by any question of allowance of claim within the meaning of section 25*a*, but rather by the question whether the pertinent provisions of the bankruptcy act, or those of sections 1906, 1907, and 1907*a* of the Kentucky Statutes (Carroll's Ky. Stat., 1909, pp. 854 to 857), are controlling."

Appellate jurisdiction in the Circuit Court of Appeals can be acquired in only three kinds of issues arising in a bankruptcy proceeding in the district court, and there are four methods of procedure for acquiring such appellate jurisdiction:

First. Issues at law, reviewable by writ of error.

Second. Controversies arising in a bankruptcy proceeding, reviewable by appeal taken under the general appellate jurisdiction of the Circuit Court of Appeals, as well as under the express authority given in section 24*a* of the bankruptcy act.

Third. Bankruptcy proceedings, which are reviewable by two methods:

(1) By a petition for superintendence and revision in matter of law under section 24*b* of the bankruptcy act.

(2) In three enumerated kinds of proceedings by an appeal under section 25*a* of the bankruptcy act as in equity, available within ten days after the rendition of the judgment appealed from.

One of the three kinds of proceedings provided for under section 24*a* is from the allowance or rejection of a claim of $500 or over.

Two questions of primary importance are pre-ented and may be stated affirmatively as follows:

First. (1) That property transferred in fraud of creditors passes as an asset of the estate to the trustee upon the bankruptcy of the fraudulent grantor under section 70*a* (4) of the bankruptcy act, and

(2) That the right of action for the recovery of such property vests exclusively in the trustee under section 70*e* of the bankruptcy act, and

(3) That property so recovered and the funds arising therefrom become assets in the hands of the trustee for distribution generally among the creditors of the bankrupt estate and are not subject to distribution only among those creditors who, in the absence of bankruptcy, could have subjected the property to their debts alone under the law of the State.

Second. That even if the property conveyed in fraud of the bankrupt's creditors is available only to those creditors who, under the State law, could have subjected the property to their debts, nevertheless, if those creditors wait until within four months of the bankruptcy before instituting their actions for recovery of the property and then have attachments levied upon the property within four months of the bankruptcy, and the lien acquired by attachment is preserved under section 67*f* of the bankruptcy act, such lien and the funds realized therefrom become a part of the general assets in the hands of the trustee for distribution among all creditors.

The property in controversy was transferred by the bankrupt about two years before the bankruptcy, and less than four months before the bankruptcy the appellants instituted their actions and had their attachments levied upon the property. The actions were brought under sections 1906 and 1907 of the Kentucky Statutes, quoted in the statement.

These statutes merely declare a cause of action for the recovery of property conveyed in fraud of creditors, following in general the statute of 13 Elizabeth. No lien exists upon the property nor is any trust impressed upon it in favor of any creditor by reason of the conveyance being fraudulent. The most that is afforded creditors under the statutes quoted is a cause of action. Section 1907*a*, Kentucky Statutes, Carroll's edition, 1903, an amendment to section 1907, quoted in the statement, is as follows:

> "That hereafter in this Commonwealth it shall be lawful for any party who may be aggrieved thereby, when any real property has been fraudulently conveyed, transferred, or mortgaged, to file, in a court having jurisdiction of the subject-matter, a petition in equity against the parties to such fraudulent transfer or conveyance or mortgage, or their representatives or heirs, alleging therein the facts showing their right of action and alleging such fraud, or the facts constituting it, and describing such property, and when done a *lis pendens* shall be created upon the property so described and suit shall progress and be determined as other suits in equity, and as though it had been brought on a return of *nulla bona*, as has heretofore been required. All laws or parts of law in conflict herewith are hereby repealed."

Before the enactment of this statute the only means of fixing a lien upon the property was by attachment. This statute provides for the creation of a *lis pendens* lien *ipso facto* the filing of the suit. The appellants, in addition to the *lis pendens* lien which arose by operation of law with the filing of their suits within four months before the bankruptcy, had attachments levied upon the same property.

The appellants' suits were filed at different times, and, although they have joined issue in bankruptcy against the trustee and general creditors, there is no apparent reason for the issuance of attachments unless it was that each bank sought to gain a preference over any other creditor who might institute suits for the setting aside of the deeds. Such

action in the absence of bankruptcy would have afforded the attaching creditors priority in the order of their attachments. Neither the statutes nor the decisions of the Kentucky courts recognize antecedent creditors as a class in the sense of being equal beneficiaries in property fraudulently conveyed.

The creditor first suing and first levying an attachment upon the property acquires a prior lien as against other creditors to whose debts the property is subject. Stamper *vs.* Hibbs, 94 Ky., 358.

In appellants' brief it is stated (p. 15):

> "*In re* Bennett (153 Fed., 673) is so comprehensive and so clearly and definitely prescribes what effect shall be given to State laws which give priority to certain debts under the provisions of the bankrupt law that we feel justified in citing that opinion in full support of our position in these cases."

The holding in the Bennett case in connection with section 64*b* (5) seems to be the foundation upon which the appellants rest their case.

The decision in *In re* Bennett involved the construction and the application in the bankruptcy proceedings of sections 2487-2488, Kentucky Statutes, Carroll's edition, 1903.

Sec. 2487:

> "When the property or effects of any (mine), railroad, turnpike, canal, or other public improvement company, or of any owner or operator of any rolling mill, foundry, or other manufacturing establishment, whether incorporated or not, shall be assigned for the benefit of creditors, shall come into the hands of any executor, administrator, commissioner, receiver of a court, trustee, or assignee for the benefit of creditors, or shall in any wise come to be distributed among creditors, whether by operation of law or by the act of such company, owner, or operator, the employees of such company, owner, or operator in such business, and the persons who shall have furnished materials or supplies for the carrying on of such business, shall

have a lien upon so much of such property and effects as may have been involved in such business, and all the accessories connected therewith, including the interest of such company, owner or operator in the real estate used in carrying on such business."

Sec. 2488:

"The said lien shall be superior to the lien of any mortgage or other incumbrance thereafter created, and shall be for the whole amount due such employees, as such, or due for such materials or supplies; that for wages coming due to employees within six months before the property or effects shall in anywise come to be distributed among creditors, as provided in section 2487, the lien of such employees shall be superior to the lien of any mortgage or other incumbrance theretofore or thereafter created; but no president or other chief officer, nor any director or stockholder of any such company shall be deemed an employee within the meaning of this article."

The Court of Appeals of Kentucky as well as the Federal courts have construed these statutes to mean that persons within the favored class have an inchoate lien which becomes fixed *eo instanti* the suspension, bankruptcy or assignment of the manufacturing or other business within the class named in the statutes, and that those liens relate back to the time of the furnishing of the materials or supplies; in other words, the one who furnishes the material and supplies does so under a contract which carries with it an inchoate lien, which lien continues for the benefit of the creditor as long as his debt remains unpaid, and upon failure of the enterprise by any of the ways provided in the statute the lien *ipso facto* the failure fixes the right of the creditor over all other classes of creditors in the property and the effects of the business. It is then necessary only for the creditor to appear in the bankruptcy or liquidating proceedings and assert his claim as a superior lien claim on the assets of the business.

Sections 1906 and 1907, Kentucky Statutes, under which the appellants proceeded, afford to the antecedent creditors only a cause of action, but make no provision for the creation or existence of any inchoate lien or trust impressed upon the property from the date of the fraudulent conveyance or from the date of the creation of their debts, nor does any lien exist for the benefit of the antecedent creditors upon the institution of their actions. By virtue of section 1907*a* upon the institution of the action for the recovery of the property if there be a sufficient description of the property sought to be recovered a *lis pendens* lien arises *eo instanti* the filing of the suit. In addition to this lien the creditor suing has the right under the general law to attach the property sought to be recovered. The appellants pursued both courses to fix liens upon the property at the instant of filing their suits, and the only liens which they ever had were the *lis pendens* lien and the attachment lien, both of which arose with the filing of their suits and within four months before the bankruptcy.

The creditors proceeding in the Bennett case and in all other cases involving sections 2487-2488, Kentucky Statutes, were for the purpose of enforcing pre-existing liens. The suits filed by the appellants in the McCracken Circuit Court were brought for the purpose of creating liens.

In Hall *vs.* Guthrie, 103 S. W. Reporter, 721, decided by the Court of Appeals of Kentucky June 28, 1907, involving sections 2487-2488, Kentucky Statutes, it is said:

> "Under these provisions where an assignment is made for the benefit of creditors a lien arises when the assignment is made; and it is immaterial that more than sixty days has elapsed after the party asserting the lien ceased to labor or furnish material, or that he has not filed his claim in the county clerk's office. The lien arises by operation of law from the assignment, although there was no lien before the assignment was made."

Further:

> "Appellant had no lien until Guthrie's Sons made the assignment. Their lien was then established by virtue of the statutes and assignment."

In Winter *vs.* Howell's Assignee, 109 Ky., 163, the court, replying to the argument that a claimant had no lien under the statutes mentioned because they were enacted after his contract was made, says:

> "This contention cannot be maintained, for the reason that the employees were given no lien until the assignment was made. Their lien arising by virtue of the assignment and not attaching to the property until it was assigned for the benefit of the creditors must be governed by the law in force when the assignment was made."

The Court of Appeals of Kentucky in two cases arising under the bankruptcy act of 1867 involving the disposition of property fraudulently conveyed by the bankrupt and recovered in actions instituted under sections 1906 and 1907, Kentucky Statutes, held that the right of recovery after bankruptcy vested exclusively in the assignee as a part of the assets in his hands for distribution. Sections 5044-5046, of the act of 1867, contained provisions similar to 70*a* (4) and 70*e* of the act of 1898.

Anderson *vs.* Anderson, 80 Ky., 638.
Starks *vs.* Curd, 88 Ky., 164.

The antecedent creditors possessed merely a right of action. This right of action could have been asserted by them at any time after their right of action arose, and had they exercised their right and subjected the property to their debts more than four months before the bankruptcy, they would have been secure in their preference. But as long as the property remained in the possession of the fraudulent vendees it remained property conveyed in fraud of creditors and upon bankruptcy vested in the trustee.

Even had neither a *lis pendens* lien nor an attachment lien been levied upon the property by the appellants, the property would nevertheless have passed to the trustee, as their actions without seizure of the property could have afforded them no advantage. As long as the property remained in the possession of the fraudulent vendees, and was in fact still property conveyed in fraud of creditors, the trustee alone had the right to have the conveyance set aside.

> "We are forced to the conclusion that the right of the trustee to prosecute this suit was not limited to the conveyance or transfer within four months previous to the filing of the petition, but that it would be the duty to attack all such conveyances antedating that period. In fact by the bankrupt act the trustee was vested with the sole power so to do." Ruhl-Koblegard *vs.* Gillespie, 61 W. Va., 584; 56 S. E., 898.
>
> Trimble *vs.* Woodhead, 102 U. S., 647.
> Moyer *vs.* Dewey, 103 U. S., 301.
> Buffington vs. Harvey, 95 U. S., 99.
> Hunt *vs.* Doyal, 57 S. E., 489 (Ga., 1907).
> Williamson *vs.* Selden, 54 N. W., 1055; 53 Minn., 73.
> Wm. H. Gray, 3 Am. Bankruptcy, 647; 62 N. Y. Supp., 618.

In Glenny *vs.* Langden, 98 U. S., 20, this court says:

> "Creditors have no remedy which will reach property fraudulently conveyed, except through the assignee, for two reasons: (1) Because all such property by the express words of the bankrupt act, vests in the assignee by virtue of the adjudication in bankruptcy and of his appointment. (2) Because they cannot sustain any suit against the bankrupt."

In Clark *vs.* Larremore, 188 U. S., 486, at page 490, this court says:

> "A different question might have arisen if the writ had been fully executed by payment to the execution creditor. Whether the bankruptcy proceedings would then so far affect the judgment and execution, and

> that which was done under them, as to justify a reconvey by the trustee in bankruptcy from the execution creditor, is a question not before us, and may depend on many other considerations."
>
> Bush *vs.* Export Storage Company, 136 Fed., 918.

In Annis *vs.* Butterfield, 58 Atlantic, 898 (Me., 1904), an action by a creditor for the recovery of property conveyed by the bankrupt in fraud of his creditors, the court says:

> "Although he has been a creditor, and before the bankruptcy proceedings were instituted might have maintained proceedings to have the conveyance set aside, yet when the bankruptcy proceedings were instituted, all his rights passed to the trustee and the power was expressly given by the statute to the trustee to avoid such transfer. After that the plaintiff as creditor has no right which he could enforce."

In re Downing, 201 Fed., 93, it is held that the bankrupt's trustee has a transferable interest in real estate owned by the bankrupt and transferred by him in fraud of creditors, although such transfer was made more than four months prior to the institution of the bankruptcy proceedings, and that the trustee may sell such interest with the right to sue and to set aside such fraudulent transaction.

It is earnestly insisted by the appellants that inasmuch as they alone, in the absence of bankruptcy, could have recovered the property for their own benefit, that the mere fact of bankruptcy should not deprive them of the fund available only to them in the absence of bankruptcy.

In First National Bank *vs.* Staake, 202 U. S., 141, precisely the same argument was made.

The facts and issues in that case are strikingly similar to those involved in the instant case. The lien obtained by the creditors claiming the priority was preserved as in this case by the order of the district court for the benefit of the bankrupt estate. In that case the bankruptcy operated to

discharge the attachment. Under the law of Virginia, the vendee of the property who held an unrecorded deed would have been vested with a good title to the property had the bankruptcy act operated only to discharge the attachment. But instead of discharging the attachment, and thereby leaving the vendee with the unrecorded deed possessed of a good title, the court of bankruptcy preserved the attachment lien under which the attaching creditors would have acquired a priority, passed that lien to the trustee for the benefit of the whole estate, and the proceeds arising from the recovery of the property came into the hands of the trustee for general distribution. (The opinion of the Supreme Court does not show the disposition subsequently made of the funds arising from the property recovery, but in fact the funds recovered were distributed generally among the creditors under orders of the referee and the district court in which the proceedings originated.)

The argument was made in that case that such operation of the bankruptcy act would have the unjust effect of depriving a certain class of creditors of advantages and benefits to which they were entitled under the State law, and that they should not be required to share property recoverable only by them with the general creditors,

> "that the bankruptcy court has nothing to do with the property, since it really did not belong to the bankrupt, and would have passed to his vendee if the attachments had not been levied on it,"

to which this court replied that to avoid such a result was one of the purposes of the bankruptcy act.

In Clark *vs.* Larremore, 188 U. S., 486, the same principle was similarly applied. There a sheriff had sold the property on execution, but before paying the money to the judgment creditor, though still within the time allowed for the return of the execution, bankruptcy proceedings were begun against the judgment debtor. It was held that the money did not

belong to the judgment creditor, and that under 67*f* the right to it passed to the trustee in bankruptcy.

The Circuit Court of Appeals considered not only the fact that the property passed to the trustee (section 70*a* (4), bankruptcy act), together with the right of action for the recovery thereof (section 70*e*, bankruptcy act), but also the fact that the appellants had seized upon the property by two liens—a *lis pendens* lien and the attachment lien—within four months, which liens, at the instance of the appellants, were preserved under section 67*f* and passed to the trustee for the benefit of the estate. The Circuit Court of Appeals did not consider alone the attachments nor base its opinion upon the rights acquired by creditors through the attachments. It is stated in appellants' brief (p. 10) "that appellants do not rest their case nor base their rights to the proceeds of the property involved upon any such claim"—*i. e.*, the attachment liens. It is inconceivable why the appellants should have procured the attachments, unless they were seeking some advantage thereby, nor why, after the bankruptcy, they should have voluntarily entered the Federal jurisdiction and sought to have the attachments preserved and passed to the trustee, unless they thereby sought some profit for themselves. It is not to be assumed, in light of their subsequent attitude, that this action was intended for the benefit of any other creditors than themselves. That the appellants conceived their hold upon the property to rest in a large measure, if not wholly, upon the attachments is shown by the emphasis placed by them upon their attachment liens throughout these proceedings until the appeal to this court. We call the attention of the court to the following pleadings filed by the appellants, in which their rights under the attachments are repeatedly reaffirmed, appearing in the record at page 34, lines 13-16; page 43, paragraphs 1 and 2; page 45, last paragraph; page 62, paragraph 2; page 68, paragraphs 1 and 2; pages 69 and 70, paragraph 1.

All of the issues as to the appellants' rights by reason of

the liens acquired by them were raised by them, and in the trial court as well as the Circuit Court of Appeals the issues so raised by the appellants and presented by them as the foundation of their rights were considered by the court. The denial that such was ever an issue or relied upon by appellants is wanting in candor and will not be countenanced by an appellate court.

> "But it is urged that as the proceeding below was a controversy between the creditor and Munsuri as to whether he was liable as a general partner, the matter before us is susceptible of being treated as a controversy arising in bankruptcy, and as distinct from a step in bankruptcy proceedings. But under the circumstances here disclosed, the contention is wanting in candor. We say this because the appeal was specifically taken from the order as one disallowing the claim of the appellees of an alleged indebtedness to them from the bankrupt firm, and such was the character necessarily attributed to the order by the judge when he entered it, and which was affixed to it by the assignment of error filed at the time the appeal was taken." Tefft, Weller & Company *vs.* Munsuri, 222 U. S., 114.

It is urged that the Kentucky Court of Appeals, in affirming the judgment of the McCracken Circuit Court setting aside the deed as fraudulent, directed the disposition to be made of the proceeds arising from the property, and that this judgment stands unmodified and unreversed and is, therefore, binding on the Federal courts in the matter of distributing the fund in bankruptcy. An analysis of this contention by the Circuit Court of Appeals in the first opinion (Record, pp. 73-82) is sufficiently clear and convincing. In considering the appeal of the trustee by which he sought specific directions to have the fund turned over to the bankruptcy court for distribution the Court of Appeals of Kentucky sustained the construction of the judgment contended for by the trustee, and said:

> "That the proceeds should be paid over to the trustee in bankruptcy to be administered as a part of the estate of the bankrupt in the bankruptcy court. In anticipation of what we assume the court will do, we may, with propriety, in this question direct that it make such orders."

At the time of the trial in the State court the antecedent indebtedness amounted to about $25,000. The property was chargeable only to the extent of the antecedent indebtedness, and on the appeal of the vendees, after disposing of the trustee's appeal, the Court of Appeals of Kentucky said:

> "As to what extent this will affect the judgment creditors we are not advised, but only those creditors whose debts were created previous to December 4, 1906 (date of delivery of deed), are entitled to participate in the proceeds realized from the sale of the property. If the proceeds amount to more than sufficient to pay such debts, the surplus should be paid to the grantees in the deed" (Record, p. 24).

It is manifest that in making the latter statement the Court of Appeals of Kentucky had in mind only that branch of the case involving the rights of the antecedent creditors and the fraudulent vendee. The context shows this, and any other construction would make the judgment contradictory and unintelligible. The failure of the Court of Appeals of Kentucky to express itself with such precision as not to admit of misinterpretation has given rise to the contention that the court, after specifically denying the right of the State court to administer the fund, then by the sentence last quoted undertook to direct the distribution. Even if the State courts of Kentucky had undertaken to direct the disposition of the fund, their orders in that respect would have no controlling force over the exclusive right of the court of bankruptcy to apply the rule of distribution of the Federal jurisdiction. The authority of the trustee in bankruptcy in the State court was to use the machinery of that court only for the purpose

of setting aside the fraudulent conveyance and converting the property when recovered into money, and the power of the State court was limited to that service. The State court was not the forum in which the creditors could have determined the rights among themselves to the distribution of this fund, although this issue was repeatedly presented by the appellants to the State courts and the State courts as distinctly avoided deciding the issue.

A distinction is observable between the attitude of the appellants in the State court and in the Federal court, and that distinction gives rise to the doubt as to the proper remedy on appeal to the Circuit Court of Appeals.

(1) In the State court the appellants contended that under the State law, the rights of action being theirs alone as antecedent creditors, they were entitled to the whole corpus of the fund and denied the right of the trustee to interfere with their recovery of the property. At the first appearance of the appellants in the Federal jurisdiction, they came for the purpose of protesting against the right of the trustee to interfere with their suits in the State court and their right to recover the property to the exclusion of other creditors (Record, p. 33, third paragraph; page 35, first paragraph).

(2) After the order of the district court preserving the liens for the benefit of the estate in bankruptcy the appellants in the bankruptcy court took the position that they were entitled to a priority in distribution of the fund to the extent of the payment in full of their debts by reason of their liens fixed upon the property (Record, p. 43, first paragraph; 45, last paragraph; 62, second paragraph; 68, first and second paragraphs; 69-70, first paragraph of replication).

Appellants now present their claim to the fund solely upon another ground. It is stated in appellants' brief:

> "The appellants' claim to preference in the distribution of the proceeds of the sale of the property which was recovered from the grantees in the deed referred to, under the judgment of the courts of the State of

> Kentucky, are based solely upon their right to recover said property which accrued when the conveyance, without valuable consideration, was executed and filed for record."

The claim now is not that the bankruptcy court has not jurisdiction to take and distribute the fund, nor that the appellants are entitled to the fund because of their liens, but that the corpus of the fund representing the property recoverable only by them under the State law in the absence of bankruptcy should, in the event of bankruptcy, be turned over to them through an order of distribution giving them a preference over other creditors.

Procedure on Appeal.

The shifting position assumed in the different courts by the appellants in this litigation gave rise to the question of remedy on appeal, which occupied so much of the attention of the Circuit Court of Appeals and was the occasion for the rendition of two opinions in the case.

The best accredited distinction between "controversy arising in a bankruptcy proceeding," appealable under section 24*a*, and "proceedings in bankruptcy," reviewable under section 24*b*, is that made by the Circuit Court of Appeals for the Sixth Circuit in *In re* Mueller, 135 Fed., 711, and approved by this court in *In re* Loving, 224 U. S., 183:

> "By controversy arising in bankruptcy proceeding is meant those independent or plenary suits which concern the bankrupt's estate and arise by intervention or otherwise between the trustee representing the bankrupt's estate and claimants asserting some right or interest adverse to the bankrupt or his general creditors."
>
> "The proceedings reviewable are those administrative orders and decrees in the ordinary course of a bankruptcy between the filing of a petition and the final settlement of the estate, which are not made especially appealable under section 25*a*. This would in-

> cludequestions between the bankrupt and hiscreditors of an administrative character, and exclude such matters are appealable under section 24*a*."

The development of the twofold aspect of this case may be briefly traced as follows:

At the time of the institution of the bankruptcy proceedings the property in controversy was in the custody of neither the trustee nor the appellants as creditors of the estate, but was in the possession of the fraudulent vendees, who were resisting alike the attacks of the appellants and the trustee. In the bankruptcy proceeding appellants filed their proofs of claim as unsecured debts. There was no objection to the allowance or disallowance of these claims as unsecured debts, and, following the custom of the referee's court, but claims stood allowed as unsecured claims. The appellants by their petitions filed before the district court (Record, pp. 33-37):

(1) Challenged the authority of the district court to interfere with their proceedings in the State court.

(2) Prayed that the trustee be directed to unite with the appellants in the State court actions for the recovery of the property.

(3) That the rights and equities acquired by the appellants through their attachment and *lis pendens* liens be fully protected and preserved.

The district court (Record, p. 36) granted the prayer to preserve the lien and did so.

After the trustee had in the State court recovered the property, and the fund arising therefrom had been paid over to the trustee, petitions were filed before the referee by the appellants, in which it was alleged that only those creditors whose debts were created previous to December 4, 1906, were entitled to participate in the proceeds arising from the sale of the property, and that all proceeds so recovered should be adjudged to and distributed pro rata among those creditors (Record, pp. 38-46).

The allegations here consist:

(1) Of the claim of the Globe Bank & Trust Company in its own behalf and that of the other two appellants of the exclusive right to the whole fund—that the corpus of the fund belonged to the antecedent creditors (Record, pp. 38-41; the claim by the First National Bank and Old State National Bank of a right to the fund by reason of their attachments as well as "by operation of law" as antecedent creditors.

(2) A prayer for an order of distribution of the fund only among the antecedent creditors.

The referee followed the general line of the appellants' pleadings in his order adjudging two classes of creditors, and that the antecedent creditors were entitled to the corpus of the fund and made an order distributing it pro rata among them, and the district court took the same view of the matter.

The question may then be resolved into these two propositions:

First. If the controversy continued as it began and is to be regarded as a controversy between the trustee on one hand and certain creditors on the other over a fund in the possession of a third party, and that without waiving any of their rights or claims to the adverse possession of the fund, that fund at the instance of the adverse claimants and with the acquiescence of the trustee was merely put into custody of the bankruptcy court pending the final determination of the rights of the trustee and the adverse claimants over the corpus of the fund, then the controversy is clearly a controversy arising in bankruptcy proceeding and cognizable under section 24*a* by the Circuit Court of Appeals and appealable to the Supreme Court in the exercise of its general appellate jurisdiction as in equity.

Second. If, on the other hand, the appearance of the appellees and their various and varying petitions be construed as a waiver of their adverse claim to the corpus of the fund

and a substitution for that contention of a claim to a preference in the right of distribution—that is, an admission by such petitions and pleas that the bankruptcy court and its trustee had a right to the possession and control of the corpus of the fund, but that the distribution of that fund in bankruptcy was governed by the rule of distribution that would have prevailed in the State court in the absence of bankruptcy, then the controversy is probably a proceeding in bankruptcy; that is, one of

> "Those administrative orders and decrees in the ordinary course of bankruptcy between the filing of the petition and final settlement of the estate, which are not made especially appealable under section 25*a*, involving only a question of law."
>
> *In re* Mueller, 135 Fed., 711.

The district court evidently took the view that the question involved was a contest over the ownership of the fund (Record, p. 36).

In the opinion of the district court it is said:

> "That the subsequent creditors having no interest in the land embraced in said conveyance under the law of Kentucky, or under the general principles of equity applicable to voluntary conveyances not actually fraudulent, there was nothing in the *lis pendens*, or in the attachments, nor otherwise, that created for such subsequent creditors any interest in the proceeds of the land" (Record, 36-37).

From this point of view this case is almost identical in essential facts with:

Knapp *vs.* Milwaukee Trust Company, 216 U. S., 545.

Hewit *vs.* Berlin Machine Works, 194 U. S., 296.

York Manufacturing Company *vs.* Cassell, 201 U. S., 344.

Security Warehousing Company *vs.* Hand, 206 U. S., 415.

> "It is therefore apparent that the mode of appeal in a given case depends upon the character of the proceeding."
>
> Coder *vs.* Arts, 213 U. S., 223.

After the action for the recovery of the property had been instituted by the trustee in a court of bankruptcy under section 70*e*, and a contest over the right of the trustee to the fund had arisen between the trustee and these adversely claiming creditors, clearly all questions affecting the fund in controversy arising as an incident thereto would have been controlled by the procedure governing the principal issues.

Coder *vs.* Arts; *In re* Loving.

Does the fact that the bankruptcy court use the machinery of the State court for the recovery of the property instead of its machinery affect the nature of the controversy between the trustee and these adverse claimants over the fund when recovered and brought into the bankruptcy jurisdiction?

If an appeal under section 24*a* was the proper method of acquiring appellate jurisdiction in this court, then an appeal from the decree of the Circuit Court of Appeals lies to the Supreme Court as a matter of right under the general appellate jurisdiction of the Supreme Court in equity, and not under the procedure laid down by section 25*b* of the bankruptcy act and general order No. 36, prescribing the manner of procedure under that section of the bankruptcy act.

Knapp *vs.* Milwaukee Trust Company, 216 U. S., 545.

Thomas *vs.* Sugarman, 218 U. S., 129.

> "A controversy arising in bankruptcy is usually presented by a contest between the trustee and the third person with respect to title to property claimed to belong to the estate. Such contests do not in every instance present a controversy arising in bankruptcy.

> Some may be determined in the bankruptcy proceedings proper. It is not always easy to distinguish between them."
>
> Loveland, 4th ed., vol. 1, 88.

The line of demarkation between the two classes of cases is indistinct, and is often exceedingly difficult, if not impossible, to distinguish.

In Duryea Power Company *vs.* Sternbergh, 218 U. S., 299, it is said:

> "It is argued that an appeal to the Circuit Court of Appeals may be treated as a petition for revision (Holden *vs.* Stratton, 191 U. S., 115), and that conversely the petition for revision may be turned into an appeal, or at least treated as one, for the purpose of an appeal to this court, if only to establish that the Circuit Court of Appeals exceeded its jurisdiction. There are two answers to this contention. In the first place, the converse proposition does not hold. An appeal opens both fact and law, and therefore might be regarded as intended to raise questions of law in any way that might be deemed proper. But the petition for revision opens only questions of law, and when the foundation of its jurisdiction is thus narrowed, the action of the court cannot enlarge it so as to deal with facts."

In Bryan *vs.* Bernheimer, 181 U. S., 188, on a writ of certiorari to the Circuit Court of Appeals for the Fifth Circuit to review an order of that court in a bankruptcy proceeding, the Supreme Court said:

> "Bernheimer appealed to the Circuit Court of Appeals, which, considering the case as if before it on a petition for revision of the decree of the district court, reversed that decree and ordered the question to be remanded."

The Supreme Court evidently approved the action of the Circuit Court of Appeals in thus considering an appeal as if it were a petition for revision, because, instead of dismissing

the writ of certiorari, it sustained the jurisdiction thereby acquired, considering the case on its merits and reversed the Circuit Court of Appeals.

Considering now the second aspect of the case as above stated, viz: That the appellees had abandoned their adverse claim to the possession of the fund and were relying only upon the proposition of law that their right of distribution fixed by the State law would be preserved in bankruptcy, and that the whole fund should be awarded to them by reason of a priority afforded under the State law—it is probable that in such a view of the case the issues between the parties constituted a proceeding in bankruptcy involving only a question of law and reviewable under section 24*b*.

In First National Bank *vs.* Chicago Title & Trust Company, 198 U. S., 280, the property in controversy consisted of goods in the actual possession of a warehouseman, and the equitable ownership of which was claimed adversely to the trustee by a bank holding warehouse receipts. The trustee filed a petition against the party in possession and the adverse claimants claiming that the property had passed to him as a part of the estate in bankruptcy, the referee held that the property was in the possession of the storage company, and that the district court was without jurisdiction. Subsequently the district court confirmed the referee's finding as to the possession, but overruled his findings as to the jurisdiction holding that the district court had jurisdiction, and then with the consent of the adverse claimants, viz., the holders of the warehouse receipts, ordered the property sold. And further held that the claimants holding the warehouse receipts were entitled to be paid out of the fund realized from the sale of the property. Thereupon the trustee appealed from said order to the Circuit Court of Appeals. The Circuit Court of Appeals decided that the storage company was not in possession of the property, and remanded the case with directions to enter a decree for the trustee. The situation then was this: If the property in controversy was not in the possession of the

storage company, then there was only a controversy between the trustee and adverse claimants over property in the possession of the trustee, and the question between them was a proceeding in bankruptcy and not a controversy arising out of a bankruptcy proceeding, and the appeal should have been dismissed. Yet the Circuit Court of Appeals treated the appeals as in fact petitions for revision. Under such circumstances if it retained jurisdiction its powers were limited to a revision of the law involved and not of facts. Therefore, if the Circuit Court of Appeals in fact regarded the appeals as petitions for revision, its attempt to reverse the district court on a question of fact, to wit the possession of the property, was an error.

The matter was taken from the Circuit Court of Appeals to the Supreme Court on certiorari, and this court assumed jurisdiction, evidently upon the theory that the appeals were treated as petitions for revision, and reversed the Circuit Court of Appeals in so far as it undertook to change the findings of fact as determined by the referee and the district court.

The points of similarity between that case and the instant case are striking. In both cases, originally, the property was in the actual possession of third parties. In that case the claimants rested their right upon the warehouse receipts representing the property. In this case, upon attachment liens levied upon the property before bankruptcy. In both cases the jurisdiction of the bankruptcy court was challenged by the claimants. Later, in both cases, by consent of the claimants, the property was sold and the fund representing it was placed in possession of the trustee in bankruptcy, without, however, waiving any rights of the claimants to the fund. (Whether that right rested upon a claim to the fund in bulk or to a right of distribution is equally difficult to determine in both cases.) In both cases the asserted claim to the fund was allowed by the district court. In that case the appeal was taken by the trustee only by an

appeal under section 24*a*; in this case relief was sought from the decree of the district court by an appeal under section 24*a* and by a petition for review. In that case the appeal was considered as if it were a petition for review, and the Supreme Court on certionari evidently approved of the action of the Circuit Court of Appeals in so regarding the appeal, otherwise it would have dismissed the writ because certiorari does not lie from an appeal proper.

In Holden *vs.* Stratton, 191 U. S., 115, certain insurance policies issued upon the life of one of the bankrupts and payable to the other bankrupt, and which had a cash surrender value, passed as assets in bankruptcy to the trustee. The policies were claimed as exempt to the bankrupts. The district court held the policies to be exempt. The trustee then filed his petition for revision to the Circuit Court of Appeals. That court held the policies not exempt and decreed a revision of the order of the district court. From that decree an appeal was taken to the Supreme Court. The appeal, upon motion, was dismissed by the Supreme Court for lack of jurisdiction. The Supreme Court says, page 118:

> "This case was not taken to the Court of Appeals by appeal, as in equity cases, to be re-examined on the facts as well as the law, nor could it have been, for it was not one of the cases enumerated in section 25*a*."

In the same opinion, page 118, in discussing section 24*a* of the bankruptcy act, prescribing a different procedure for acquiring appellate jurisdiction in certain enumerated proceedings in bankruptcy which are excepted from the general class of proceedings in bankruptcy referred to in section 24*b*, the court says:

> "The allowance of a debt or claim is a part of the bankruptcy proceedings, and not an independent suit, and under the act of 1867 it was held that this court had no jurisdiction to review judgments of the circuit courts dealing with the action of the district courts in such allowance or rejection, because they were not final. Wiswall *vs.* Campbell, 98 U. S., 47; Leggett

> *vs.* Allen, 110 U. S., 741. The jurisdiction now given is carefully restricted and cannot be expanded beyond the letter of the grant. It is an exception to the general rule as to appeals and writs of error obtaining from the foundation of our judicial system." McLish *vs.* Roff, 141 U. S., 661.

In Bryan *vs.* Bernheimer, 181 U. S., 188, the assignee under a deed of assignment made pursuant to a State law, and before the bankruptcy, sold to Bernheimer, after the institution of the bankruptcy proceedings and when Bernheimer had knowledge of the proceedings, a part of the property which came into the hands of the assignee. The petitioning creditors and the marshal sought, by an action instituted in the district court, to recover from Bernheimer the property which he had so bought and paid the assignee for, and that Bernheimer be required to account for the value of the goods which he had already disposed of. Bernheimer admitted the possession of the goods by him, but plead no adverse right of possession; that the amount which he had paid for the goods to the assignee had passed to the trustee, and that he should either be allowed to keep the goods, or the trustee should be required to pay back to him the amount paid by him to the assignee and he be permitted to return the goods or their value to the trustee.

The district court adjudged that Bernheimer had acquired no title to the goods nor to the proceeds of the sales made by him, and directed him to pay to the marshal all proceeds so realized by him from sales of the goods. Bernheimer appealed to the Circuit Court of Appeals,

> "which considering the case as if before it on a petition for revision of a decree of the district court, reversed that decree and ordered the question to be remanded to that court with instructions to dismiss the petition against Bernheimer."

The marshal thereupon obtained a writ of certiorari from the Supreme Court. The Supreme Court entertained juris-

diction and considered the case on its merits. In the opinion the court says, page 194:

> "The present case involves no question of jurisdiction over a suit by a trustee against a person claiming an adverse interest in himself."

Page 197:

> "Moreover, the consent of the proposed defendant, Bernheimer, to this mode of proceeding, is shown by the terms of his claim, in which, not protesting against the jurisdiction of the court of bankruptcy, he expressly submitted his claim to that court, and asked for such orders as might be necessary for his protection."

Assuming that the claimants had abandoned their adverse claim to the corpus of the fund, and were claiming the right of protection under an order of distribution in bankruptcy, then the facts in Bryan *vs.* Bernheimer are similar to those of the instant case. The question then resolved itself in the Bernheimer case into one of law only, to wit: the making of an order which would afford him substantial justice.

In the instant case, assuming the issues as above stated, there would be no question of adverse claim to a fund, but only the making of an order determining the right of the claimants in the fund in the possession of the bankruptcy court—that is, whether those rights are governed by the State or bankruptcy rule of distribution, and whether the claimants have any greater right to the fund than the trustee and general creditors.

On the Rule of Distribution.

By whatever means the fund may have been recovered, after it was paid into the bankrupcy court the disposition of the fund is determined by the rules of distribution prevailing under the bankruptcy law and not under the State laws operative if bankruptcy had not intervened. The mission

and authority of the trustee to enter the McCracken Circuit Court were simply to recover such funds as were open to recovery on the part of creditors of the bankrupt.

Acme Harvester Company *vs.* Beekman Lumber Company, 222 U. S., 307.

First National Bank *vs.* Staake, 202 U. S., 141.

Miller *vs.* New Orleans Fertilizer Company, 211 U. S., 496.

In the last case the question arose in a bankruptcy proceeding against a copartnership, touching the distribution of assets belonging to one of the individual members of the firm. It was pointed out by the present learned chief justice that while under the law of Louisiana the creditors of a partnership are as to firm assets given preference over creditors of individual members of a firm, yet that partnership creditors and creditors of the individual partners have equal rights in the individual assets. Of course this last feature is opposed to the corresponding feature of the bankruptcy act. The trustee in bankruptcy brought an action in a State court to annul any transactions affecting the property of the bankrupts, and to recover judgment for the benefit of the bankrupt estate. Certain other actions were then pending in the State court to recover upon claims held against the firm and for the further purpose of having certain sales of property set aside and the proceeds applied to the payment of their claims, which sales had been made by one member of the firm of his individual property. The trustee was by order of the State court substituted as party plaintiff in those suits in his capacity as trustee of the bankrupt estate. In the course of the opinion it was said (505):

> "Assuming, therefore, that the trustee was properly authorized, it follows that he was entitled to preserve and enforce the privilege or lien, which arose in favor of the creditors, resulting from their pending action, even although the cause of action

> arose from the State law, and the application of that law was essential to secure the relief sought. To the accomplishment of this end the bankrupt law was cumulative and did not abrogate the State law."

Recalling the difference between the law of Louisiana and the bankruptcy act touching the distribution of assets belonging to individual members of a Louisiana partnership, the following we think is controlling (506):

> "In view of the distinction between the estate of partnerships and the estates of the members of the firm, which is made by the bankrupt law, and the method of distinction for which that law provides, of course the trustee will hold the fund as an asset of the estate of the individual member, and primarily for the benefit of his creditors."

Further, upon the question of distribution, the learned justice recognized the power of the State court to pass upon the question of preference, but denied its right to determine what creditors were to participate in the distribution. He said (506):

> "The one (the question of preference) was within the province of the State court for the purpose of the case before it; the other (the matter of distribution) was a different question, depending upon independent considerations exclusively cognizable in the bankruptcy court;"

and since the State court had itself so decided, its judgment was affirmed.

Section 64*b* (5) of the bankruptcy act has no application to the question involved in these appeals. Section 64*b* (5) was intended to preserve in bankruptcy the priorities in payment afforded creditors by the State laws. It was not intended to afford any creditor the right to appropriate a cause of action to recover property conveyed in fraud of creditors nor to appropriate by an order of distribution in

bankruptcy the proceeds arising from such property when recovered by the trustee. Sections 70*a* (4) and 70*e* of the act expressly negative such intent.

It is not our contention that the Circuit Court of Appeals erred in assuming jurisdiction in the appeal and deciding this case as it did. In fact, as intimated by this court in several of the cases above cited, the Circuit Court of Appeals perhaps had the right in the appeal to consider those questions of law which might have been brought up to it in the revisory proceeding, but the question of practice being involved in some doubt as stated by the Circuit Court of Appeals, the petition for the writ of certiorari is brought to this court as a measure of protection to the appellees.

Respectfully submitted,

W. F. BRADSHAW, JR.,
BRADSHAW & BRADSHAW,
Attorneys for the Appellee and Petitioners for Writ of Certiorari.

J. D. MOCQUOT,
Of Counsel.